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No. 90-98

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1990

GEORGE FRANKLIN, *et al.*,
Petitioners,

v.

PEAT MARWICK MAIN & CO., *et al.*,
Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

BRIEF IN OPPOSITION OF RESPONDENT KPMG PEAT MARWICK

Of Counsel:

LEONARD P. NOVELLO
General Counsel
JOHN A. SHUTKIN
Associate General Counsel
KPMG PEAT MARWICK
767 Fifth Avenue
New York, NY 10153

J. ANTHONY SINCLITICO, III
MARK J. MCKEON
GIBSON, DUNN & CRUTCHER
750 "B" Street, Suite 3300
San Diego, CA 92101-4605

*THEODORE B. OLSON
TERENCE P. ROSS
GIBSON, DUNN & CRUTCHER
1050 Connecticut Avenue, N.W.
Washington, D.C. 20036-5303
(202) 955-8500

**Counsel of Record*

Attorneys for Respondent KPMG Peat Marwick

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PRESS OF BYRON S. ADAMS, WASHINGTON, D.C. (202) 347-8203

QUESTIONS PRESENTED

Petitioners brought private class actions for damages under various federal securities laws. As a part of a settlement between petitioners and some of the defendants, the settling parties sought an order barring the nonsettling defendants' statutory contribution rights against the settling defendants. The United States Court of Appeals for the Ninth Circuit held that the contribution rights of the nonsettling defendants could be satisfied and thus extinguished prior to trial only by an order limiting the liability of the nonsettling defendants to the proportion of the total liability for which they were collectively responsible. In this context, the petition raises the following questions:

1. Whether and under what circumstances a nonsettling defendant's statutory right to contribution from co-defendants in a private action for damages under federal securities laws may be extinguished prior to trial as a part of a settlement between plaintiffs and some defendants; and

2. Whether there is an implied right of contribution available to a defendant sued under Section 10(b) of the Securities Exchange Act of 1934 and/or under Section 12(2) of the Securities Act of 1933.*

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* On January 1, 1990, respondent formally changed its name to KPMG Peat Marwick. KPMG Peat Marwick is a partnership without any parent, subsidiaries or affiliates.

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BRIEF IN OPPOSITION OF RESPONDENT KPMG PEAT MARWICK

STATEMENT OF THE CASE

A. Introduction

The United States Court of Appeals for the Ninth Circuit was presented in this case with an issue not previously decided by any federal appellate court. The petitioners had brought federal securities class actions against the issuer of certain securities, its officers and directors, and its auditor and underwriter. Petitioners thereafter entered into a settlement with the insider defendants—the issuer and its directors and officers. As a part of the settlement, in order to provide a full release to the insider defendants,

the settling parties sought and received a District Court order extinguishing the statutory contribution rights of the nonsettling defendants against the settling defendants.

The Ninth Circuit determined that the District Court could properly accommodate the request for a full and final release of the settling defendants only through an order that protected the statutory rights of the nonsettling defendants to contribution from their co-defendants. The court found that those contribution rights could be satisfied prior to trial only by an order limiting the ultimate liability of the nonsettling defendants to their proportionate culpability as determined at trial. In this manner, the Ninth Circuit preserved the rights of defendants under the federal securities laws and the policies underlying those laws while also allowing the plaintiffs the opportunity to effectuate a partial settlement with selected defendants.

The Ninth Circuit's resolution of the issue presented to it was in perfect harmony with the concepts of joint and several liability and contribution that form an interdependent structural component of the federal securities laws. Consistent with that structure, it also facilitated the desire of plaintiffs to settle with and release from further liability the defendants with whom they had reached terms. The Ninth Circuit's resolution of the issue presented to it did not conflict with any other circuit court decision because no other federal appeals court has ever considered and resolved the same issue.

The second question presented by the petition was not considered or resolved by the Ninth Circuit because it was not presented to it.

The third question presented by the petition is properly subsumed within the first question and need not be considered separately.

B. Proceedings Below

This class action is comprised of six cases consolidated in the United States District Court for the Southern Dis-

trict of California as *In re Kaypro Shareholders Securities Litigation*. The petitioners (plaintiffs below) allege violations of the Securities Act of 1933, 15 U.S.C. §§ 77a, *et seq.* (the "1933 Act"), and the Securities Exchange Act of 1934, 15 U.S.C. §§ 78a, *et seq.* (the "1934 Act"), as well as state securities laws (California Corporations Code §§ 25500, *et seq.*) and state common law.

Petitioners were purchasers between August 25, 1983, and July 17, 1984, of the common stock of Kaypro Corporation. The defendants include Kaypro Corporation and eight of its directors and officers (the "Kaypro Defendants"); respondent KPMG Peat Marwick ("Peat Marwick"), Kaypro's outside independent auditor; and respondent Prudential-Bache Securities Inc. ("Bache"), Kaypro's investment banker and the lead underwriter for Kaypro's initial public stock offering.[1]

In 1987, petitioners and the Kaypro Defendants entered into a Stipulation of Settlement, Petition ("Pet.") Appendix ("App.") at 35a-66a, pursuant to which the claims against the Kaypro Defendants would be released in exchange for $9.25 million, slightly less than half their $20 million insurance coverage. Pet. at 4. Among other things, the terms of the Stipulation of Settlement required that the settling parties seek an order from the District Court extinguishing any claims for contribution against the settling defendants possessed by Peat Marwick and Bache, the nonsettling defendants. Pet. App. at 49a.

On February 1, 1988, the District Court approved the Final Judgment and Order of Dismissal and related orders in the form submitted by the petitioners, Pet. App. at 25a-34a, ordering, *inter alia*, that "[a]ll claims for contribution, indemnification, or reimbursement, however denominated, against the Settling Defendants arising under the federal

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[1] Peat Marwick and Bache will be referred to collectively as the "nonsettling defendants."

securities laws or state law . . . in favor of persons, including Non-Settling Defendants . . . based upon the Settled Claims, are extinguished, discharged, satisfied and/or otherwise unenforceable." Pet. App. at 33a.

The District Court received no evidence on the issue of the relative culpability or fault of the Kaypro Defendants or the nonsettling defendants. The only evidence before the court was a declaration of petitioners' counsel supporting the conclusion that the settlement was made and entered into in good faith. This declaration consisted of numerous newspaper articles, Kaypro's securities filings and petitioners' damage calculations. Therefore, although the court found that the settlement had been entered into in good faith and was reasonable in amount from the standpoint of the class members, the court did not purport to determine the relative culpability of the Kaypro Defendants vis-a-vis the nonsettling defendants.

The nonsettling defendants appealed. They contended that because contribution must be based on the actual relative culpability of the parties, *Smith v. Mulvaney*, 827 F.2d 558, 561 (9th Cir. 1987), a nonsettling defendant's right to contribution could not be eliminated prior to a trial or an adjudication determining the defendant's relative culpability.

The Ninth Circuit determined that the issue whether and under what circumstances a nonsettling defendant's rights to contribution could be extinguished prior to trial as a part of a partial settlement in a federal securities case was a "question of first impression." *Franklin v. Kaypro Corp.*, 884 F.2d 1222 (9th Cir. 1989) *reproduced in* Pet. App. at 1a, 8a.[2] The court considered and rejected

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[2] The court below distinguished cases under federal securities laws, where there is a "statutorily created right to contribution," from actions under other federal laws that do not create such a right. 884 F.2d at 1228, n.10, Pet. App. at 14a, n.10. The court did not, however,

the nonsettling defendants' argument that their statutory rights to contribution could not be "satisfied prior to a full trial," *id.* at 1229, Pet. App. at 15a, and turned to the more difficult question of the circumstances under which those rights could be satisfied and extinguished as a result of a settlement between the petitioners and some of the defendants.

The Ninth Circuit examined the nonsettling defendants' statutory right of contribution as balanced against the settling defendants' desire for a complete release. The court considered, but rejected, an approach that would extinguish the contribution rights of the nonsettling defendants in exchange for an offset against any subsequent judgment in the amount of the settlement. *Id.* at 1230, Pet. App. at 17a-19a. The court felt that this approach would permit plaintiffs in securities cases to settle for small amounts with the most culpable defendants and leave the least culpable but most solvent defendants facing the greatest exposure. This would frequently result in the nonsettling defendants paying more than their share of culpability in violation of the comparative fault principles underlying the equitable right to contribution.

The Ninth Circuit determined that it could preserve fully the rights of the nonsettling defendants to contribution and yet permit the settling defendants a full and final release from exposure to liability by providing that the nonsettling defendants' liability would be limited to the portion of liability for which the nonsettling defendants were responsible as determined at trial. The nonsettling defendants would continue to be jointly and severally liable for that remaining percentage, and would continue to have

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distinguish between the right to contribution under Section 11 of the 1933 Act, which is expressly articulated in Section 11, and the right to contribution that may be implied under Section 12 of the 1933 Act or Section 10(b) of the 1934 Act as a corollary to the private right of action also implied from those provisions. *See infra* notes 19 & 20.

contribution rights against each other. *Id.* at 1231, Pet. App. at 20a.

The Ninth Circuit remanded to the District Court so that the District Court could refashion its order extinguishing the contribution rights of the nonsettling defendants to add the provision that the liability of the nonsettling defendants would be limited to their actual percentage of liability for the amount of total damages as determined at trial. *Id.* at 1232, Pet. App. at 23a.

SUMMARY OF ARGUMENT

The Ninth Circuit's approach to the preservation of contribution rights created by statute in favor of defendants in federal securities cases, while simultaneously permitting a partial settlement with some defendants and a full release of the settling defendants from those contribution claims, was reasonable and not at variance with any decision by any other federal court of appeals. The Ninth Circuit believed it was dealing with a question of first impression and, in fact, no other federal court of appeals has yet had an opportunity to address the issue.

The Second Circuit decision cited by petitioners as conflicting with the decision below did not involve the evaluation of the pretrial extinguishment of rights to contribution under federal securities laws. In fact, the issue of contribution did not arise in that case in any context and was not even mentioned by that court. Moreover, when examined carefully, it is apparent that the "one satisfaction rule" that was at issue in the Second Circuit case is not necessarily incompatible with the Ninth Circuit's analysis in this case. A court could extinguish the contribution rights of nonsettling defendants by reducing any subsequent judgment against them by the greater of the dollar amount of the prior settlement or by the percentage

of liability of the settling defendants. That approach would honor both the Ninth Circuit's proportionate liability analysis of contribution rights *and* the Second Circuit's one satisfaction rule for offsets of prior settlements. In short, not only do the two circuit court decisions address different questions from different perspectives, but they are capable of being harmonized. There simply does not exist the type of conflict among the circuits that would warrant the invocation of this Court's jurisdiction.

The decision below is a reasoned and rational balancing of statutorily created rights to contribution with the interest of some plaintiffs in some cases to settle with less than all defendants. It does not, as petitioners contend, abrogate joint and several liability, but merely recognizes joint and several liability and contribution as equally important concepts, both of which are entitled to protection by the courts.

And the Ninth Circuit decision does not discourage settlements. It might, under some very limited circumstances, cause a plaintiff to evaluate more carefully some *partial* settlements, but only in those cases where a plaintiff might wish to release a highly culpable party in order to secure funds to litigate against a less culpable but more financially accountable defendant. Global settlements will, in fact, be encouraged by the Ninth Circuit's decision, and plaintiffs in securities cases will retain full control over the settlements they choose voluntarily to negotiate.

Petitioners' second question was not properly presented to the courts below, was not ruled upon below, and is not properly before this Court. Moreover, it does not raise an issue or issues that have been addressed in a directly conflicting manner by the federal courts of appeal. Petitioners' third question is not a separate legal issue and should be resolved in the same manner as their first question.

REASONS WHY THE PETITION SHOULD BE DENIED

I

THE FIRST QUESTION PRESENTED IS NOT A SOURCE OF CONFLICT AMONG THE CIRCUITS

The first question presented in the petition is whether and under what circumstances the statutory contribution rights of defendants in federal securities cases may be released, satisfied or extinguished as a part of a court order approving a settlement between the plaintiff and some of the defendants. This was an issue of first impression for the federal courts of appeals.

Contrary to petitioners' claim, the Ninth Circuit's decision does not conflict with *Singer v. Olympia Brewing Co.*, 878 F.2d 596 (2d Cir. 1989), *cert. denied*, ___ U.S. ___, 110 S. Ct. 729 (1990). The insubstantiality of petitioners' argument that there is such a conflict is revealed by petitioners' decision to confine that argument to a single sentence at the beginning of Part II A 1 of their petition. Petitioners assert that *Singer* conflicts with the decision below, but do not discuss a word of the facts of *Singer* and hasten immediately into a discussion of assertedly conflicting district court decisions. That is because the *Singer* case is not at all inconsistent with the Ninth Circuit's decision in this case, as any close scrutiny of it readily reveals, and, in fact, does not have anything whatsoever to do with rights to contribution.

In *Singer*, the plaintiff brought suit against Olympia Brewing Co. (the "Olympia case") for violation of various antifraud provisions of the federal securities laws and for claims under the Racketeer Influenced and Corrupt Organizations Act ("RICO"). The RICO claim, however, was dismissed prior to trial. Singer also commenced a similar action in the same court against Loeb Rhoades & Co. (the "Loeb Rhoades case") for injuries resulting from the same events. That action was subsequently transferred to

another district court where, in contrast to the Olympia case, the RICO claim survived a motion to dismiss. The Olympia case went to trial and the jury returned a verdict for Singer and judgment was entered in the amount of $2,958,350.50. Two weeks later, Loeb Rhoades paid $1,250,000 to settle the claim against it in the other case. The court in the Olympia case thereupon set off the $1,250,000 settlement paid by Loeb Rhoades against the $2,958,350.50 jury verdict rendered against Olympia.

On appeal, Singer argued that the setoff was improper because Loeb Rhoades had settled not only identical securities law claims, but also the RICO claim (with its treble damages provisions) that had been dismissed from the Olympia case. Singer argued that where a plaintiff may be entitled to more damages from one defendant than another, a settlement with one defendant should be deducted not from the amount recovered after trial against the nonsettling defendant, but from the highest amount of "provable damages" that could have been recovered from the settling defendant. 878 F.2d at 600. The Second Circuit rejected Singer's argument, concluding that it "border[ed] on the frivolous." *Id.* Singer's position was contrary to the well-established rule that the settlement amount should be "deducted from the claim or judgment in the litigated case, and not from the potential claim or judgment in the settled case." *Id.* at 601. The Second Circuit upheld the offset applied by the District Court, ruling that, in the context of *Singer*, the "one satisfaction rule" required that the injury recovered in a judgment be reduced by the amount already recovered for the same injury in a settlement with another defendant so that a plaintiff would recover "only one satisfaction for each injury." *Id.* at 600.

Thus, *Singer* is wholly inapposite to the question presented to the Ninth Circuit in this case. The appellant in *Singer* conceded the applicability of the "one satisfaction rule," *id.*, did not seek an allocation of damages based on

relative fault, and did not raise the issue of contribution between co-defendants. Apparently, neither Loeb Rhoades nor Olympia raised the issue of their respective rights to contribution. In contrast, the Ninth Circuit was presented with a partial settlement of a single lawsuit and how to balance the nonsettling defendants' statutory rights to contribution against the plaintiffs' and the settling defendants' desire to extinguish those rights as a part of their settlement.

Although the *Singer* decision does apply the "one satisfaction rule" and affirms the direct deduction of Loeb Rhoades' settlement from Singer's judgment against Olympia, this was a correct and unremarkable result given the fact that all parties conceded the applicability of that rule.[3] Olympia apparently remained free to bring an action against Loeb Rhoades to vindicate its right to contribution. The *Singer* court was *only* concerned with whether the settlement should be deducted from the judgment or from the amount of the settling defendant's potential liability.

There is yet another, more fundamental, reason why *Singer* is not in tension with this case. *Singer* focused on the "one satisfaction rule." That rule, which places a ceiling on plaintiff's recovery, is not necessarily incompatible with the Ninth Circuit's decision in this case. The Ninth Circuit held that after trial the liability of the nonsettling defendants will be limited to "the percentage of the total amount for which they are responsible." 884 F.2d at 1231, Pet. App. at 20a. Applying the same analysis and rationale as the Ninth Circuit, another court could determine that the liability of the nonsettling defendants as determined at trial would be reduced by the dollar-for-dollar amount

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[3] In fact, in a previous case where no settlement bar order was at issue, the Ninth Circuit held in accord with *Singer* that a payment made by a joint tortfeasor would reduce the claim against the remaining tortfeasor on a dollar-for-dollar basis. *Seymour v. Summa Vista Cinema, Inc.*, 809 F.2d 1385, 1389, *modified*, 817 F.2d 609 (9th Cir. 1987).

of the settlement or the amount of the settling defendants' share of the damages, *whichever is greater*. This approach would respect the equitable principle of comparative fault for contribution claims as articulated by the Ninth Circuit, but would also be faithful to the one satisfaction rule.[4]

In fact, as discussed in greater detail *infra*, an amalgamation of the comparative fault principle and the one satisfaction rule was precisely the solution actually negotiated between the petitioners and the settling defendants as a fallback in the event that the terms of their settlement had not been approved by the court of appeals. They expressly agreed that if the nonsettling defendants were to appeal successfully in this case, the settlement would remain binding and "convert to a reduction in judgment settlement" whereby any judgment subsequently entered against a nonsettling defendant "would be reduced by the amount of the Settlement . . . or by the amount of the Settling Defendants' share of the damages, *whichever is greater*." Pet. App. at 55a-56a (emphasis added).

Thus, *Singer* and the Ninth Circuit's decision are not in conflict because they dealt with different issues from entirely discreet perspectives. Moreover, a federal appellate court could readily adhere to the rationales underlying each of the decisions. Indeed, the petitioners have recognized this by incorporating the principles of both *Singer* and the Ninth Circuit's decision below in their settlement agreement in this case.

Petitioners also mistake various other circuit court decisions as conflicting with the decision below in this case. Those decisions, however, were either not decided under the federal securities laws or did not involve an attempt to extinguish the contribution rights of nonsettling

[4] The Ninth Circuit was not prepared to go this far, as its decision makes clear, 884 F.2d at 1231-32, Pet. App. at 21a-22a, but its decision in this case did not require it to do so. It is perfectly possible that if the right circumstances were presented, the Ninth Circuit, or another court, would do so.

defendants.[5] Therefore, those courts were not required to resolve a conflict between the statutory right to contribution established in the federal securities laws and a request that contribution claims be extinguished as a part of a partial settlement.

Implicitly recognizing that close scrutiny of *Singer* would reveal that there was no conflict among the circuits, petitioners instead concentrate their attention on three district court decisions that purportedly apply conflicting approaches and, based on these district court decisions, argue that "the Circuits [are] badly split on this important issue." Pet. at 16. One of these decisions, however, was handed down prior to the Ninth Circuit's decision in *Franklin* and, thus, was rendered without benefit of the Ninth Circuit's analysis of the issue and its well-crafted solution.[6] Petitioners acknowledge that another of the decisions[7] "does not present precisely the same issue as presented here, as the district judge determined that the liability of the co-defendants may not have been joint and several." Pet. at 19, n.13. And the third district court decision mentioned by petitioners[8] manifestly failed to come to grips with the fundamental differences between *Singer* and this case—specifically, the fact that *Singer* did not involve the attempted pre-trial extinction of contribution rights.

At most, it can be said that the first question presented by this petition is an issue of first impression in the federal

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[5] *Miller v. Apartments & Homes of New Jersey, Inc.*, 646 F.2d 101 (3d Cir. 1981) (civil rights action); *Gould v. American-Hawaiian Steamship Co.*, 535 F.2d 761, 784 (3d Cir. 1976) (securities law violations, but no application for the extinguishing of contribution rights); *Screen Gems—Columbia Music, Inc. v. Metlis & LeBow Corp.*, 453 F.2d 552 (2d Cir. 1972) (copyright infringement action).

[6] *In re Atlantic Financial Management Inc. Securities Litigation*, 718 F. Supp. 1012, 1018 (D. Mass. 1988).

[7] *In re Terra-Drill Partnerships Securities Litigation*, 726 F. Supp. 655 (S.D. Tex. 1989).

[8] *Dalton v. Alston & Bird*, Civ. No. 85-4302 (S.D. Ill. May 24, 1990).

courts of appeals that is just beginning to be addressed in the district courts.[9] It remains unclear whether the Ninth Circuit's approach will be adopted or modified by other circuit courts or whether the sort of rigorous judicial examination of the issue that can only come from additional decisions by the federal courts of appeals will yield some alternative approach. In either event, this question should not be accepted by the Court at this time.

II

THE NINTH CIRCUIT PROPERLY BALANCED STATUTORY RIGHTS TO CONTRIBUTION WITH THE OTHER GOALS OF THE SECURITIES LAWS AND THE POLICY OF ENCOURAGING SETTLEMENTS

Petitioners repeatedly insist that the Ninth Circuit's decision "revokes" joint and several liability, handicaps victims of securities fraud, and will discourage the settlement of complex securities litigation. None of these contentions is accurate.

A. The Ninth Circuit's Decision Does Not Modify Principles Of Joint And Several Liability

Contribution is an equitable principle that is an integral part of the doctrine of joint and several liability. Contribution was originally developed to mitigate the harsh results of joint and several liability. Note, *Apportioning Contribution Shares Under the Federal Securities Laws Act: A Suggested Approach for an Unsettled Area*, 50 Fordham L. Rev. 450, 456 (1981). The intimate relationship between joint and several liability and contribution is best demonstrated by the fact that the two correlative rights

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[9] Indeed, it appears that the first time this issue was ever addressed definitively in a securities case in the district courts was in 1987 in *In re Nucorp Energy Securities Litigation*, 661 F. Supp. 1403 (S.D. Cal. 1987).

appear in the same sentence in Section 11(f) of the 1933 Act:

> All or any one or more of the persons specified in subsection (a) of this section shall be jointly and severally liable, and every person who becomes liable to make any payment under this section may recover contribution . . . from any person, who, if sued separately, would have been liable to make the same payment . . . .

15 U.S.C. § 77k(f). Thus, Congress inextricably linked the joint and several liability created under Section 11 with the right to contribution among the parties who are made jointly and severally liable by that section.

Rights of joint and several liability and rights of contribution are just as interdependent, at least conceptually, where those rights are implied, as from Section 10(b) of the 1934 Act.[10]

Petitioners ignore the inherent connection between joint and several liability and the right to contribution. They urge that the nonsettling defendants' express right to contibution under Section 11 may be abrogated as a consequence of petitioners' decision to settle with other defendants in order to preserve petitioners' Section 11 right to joint and several liability. The securities laws, however, create no such preference in favor of a plaintiff's right to joint and several liability over a defendant's right to contribution.

The Ninth Circuit recognized that it need not repeal the right to contribution in order to facilitate petitioners' partial settlement. The court upheld the settlement and the release of the settling defendants. Once petitioners choose to pursue this course, however, their ability to recover the entire judgment sought in the action would potentially be affected adversely if they failed to assess properly the

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[10] *See infra* note 20.

settling defendants' potential level of culpability. The doctrine of joint and several liability is thus only affected by the Ninth Circuit's decision to the extent that an equitable condition is imposed on the granting of petitioners' request to extinguish the nonsettling defendants' equitable rights. That equitable limitation is necessary to preserve the nonsettling defendants' right to contribution.[11]

It is important to stress that the Ninth Circuit's restriction on the right to contribution *and* the concomitant limitation on the liability of the nonsettling defendants is triggered only when a plaintiff settles voluntarily on terms it deems fair and reasonable and affirmatively seeks a judicial order stripping the nonsettling defendants of their contribution rights as a part of the settlement. The Ninth Circuit decided that since the contribution rights are based "on the actual relative culpabilities of the tortfeasors," 884 F.2d at 1226, Pet. App. at 9a, the satisfaction of those rights before trial must be based on the same principle. Plaintiffs do indeed then run some risk if they seriously misassess the settling defendants' proportional culpability, but it is a risk they voluntarily assume and one that they can choose to avoid if they deem it to be too great.

If plaintiffs are fearful that a highly culpable defendant may be offering an inadequate amount to settle, they need not enter into the settlement or they can avoid a settlement that purports to contract away the rights of the nonsettling defendants.

B. The Ninth Circuit's Decision Does Not Inhibit or Weaken the Rights of Victims of Securities Fraud

The victims of securities fraud are not disadvantaged under the Ninth Circuit's decision. They retain complete

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[11] In fact, as among nonsettling defendants, the Ninth Circuit decision recognizes that they would continue to be jointly and severally liable for the percentage of the total amount for which they are collectively responsible, and would also continue to have rights of contribution against one another. 884 F.2d at 1231, Pet. App. at 20a.

control over whether they will settle, with whom, and under what terms. If they wish to settle with an impecunious defendant who played a substantial role in the fraud, they can decline to grant the settling defendant a release from contribution claims. A defendant without resources is not likely to have a strong interest in being relieved of liability for such claims in any event. At bottom, a plaintiff can decline to settle if the settlement will have an adverse impact on the potential recovery.

Petitioners' emphasis on the rights, perspective and interests of plaintiffs in securities cases overlooks the fact that the same law that creates Section 11 liability created the defendants' right to contribution. The right of the defendants to contribution is as important under the law as the plaintiffs' right to joint and several liability. The same is true as to Section 12 of the 1933 Act and Section 10 of the 1934 Act. If the Courts imply private causes of action imposing joint and several liability and then also imply a right to contribution under these provisions, both sets of rights must be accorded co-equal status.

Petitioners' exclusive emphasis on the interests of allegedly defrauded shareholders also ignores other fundamental purposes of the federal securities laws which are protected by the Ninth Circuit decision. Thus, the potential for collusive and inadequate settlements with the most culpable parties, inherent in the *pro tanto* rule, reduces the deterrent effect of the civil damage remedy. Moreover, imposition of liability upon institutions, such as accounting firms, in an amount grossly disproportionate to their secondary role in the securities registration and reporting process, will clearly impair the efficient formation of capital for public companies, an additional goal of the federal securities laws. *See generally* Testimony of Richard C. Breeden, Chairman, U.S. Securities and Exchange Commission, U.S. Senate Committee on Banking, Housing and Urban Affairs, July 19, 1990, 1-3. The long-run effect of such disproportionate liability is to increase the cost of an

accountant's services and to increase the cost of offering securities. Inescapably, the cost of raising capital increases and the nation's "economic muscle" weakens. *Id.*

C. The Ninth Circuit's Decision Is Consistent With Modern Comparative Fault Principles And Promotes Global Settlements

Because this dispute revolves around the rights of defendants to contribution after a partial settlement in securities cases, it is useful to consider the development over the last fifty years of modern settlement-bar rules. Over that time, three approaches have been employed by the courts to address different aspects of the subject: the *pro rata* method, the *pro tanto* method (urged here by petitioners), and the "proportional culpability" method applied by the Ninth Circuit in this case.

Under the *pro rata*, or "equal shares," method, a defendant's liability is determined strictly according to the number of defendants in the lawsuit by dividing the total judgment by the number of tortfeasors. This method was adopted in the 1939 version of the Uniform Contribution Among Tortfeasors Act (the "1939 Uniform Act"), the first of three related model acts developed by the National Conference of Commissioners on Uniform State Laws ("NCCUSL").[12] Under the 1939 Uniform Act, discharge of a settling defendant was conditional on the plaintiff agreeing to give the nonsettling defendant a *pro rata* credit.

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[12] Petitioners mistakenly suggest that the 1939 Uniform Act utilized a "proportional fault" approach, and it was this approach that was rejected by the drafters of the 1955 version of the Uniform Contribution Among Tortfeasors Act. Pet. at 20, n.14. That is not correct. Section 5 of the 1939 Uniform Act provides: "Release; Effect on Contribution.—A release by the injured person of one joint tortfeasor does not relieve him from liability to make contribution to another joint tortfeasor unless the release . . . provides for a reduction to the extent of the pro rata share of the released tortfeasor, of the injured person's damages recoverable against all the other tortfeasors." 1939 Uniform Act § 5. *See generally* Note, *Settlement in Joint Tort Cases*, 18 Stan. L. Rev. 486 (1966) (hereinafter, "Stanford Note").

Id. at § 5. Among its many drawbacks, the amount a defendant pays under the *pro rata* method is arbitrarily based on the number of defendants and the rule may accordingly be highly inequitable in its application.

The *pro tanto* approach to settlement credits grants the nonsettling defendant a dollar-for-dollar credit of the settlement amount, and the settling defendant is released from further liability for contribution to the nonsettling defendants. This method, favored by petitioners, is the method adopted in the 1955 version of the Uniform Contribution Among Tortfeasors Act. *Unif. Contribution Among Tortfeasors Act* (1955 revision), 12 U.L.A. 63 (1975) (the "1955 Uniform Act").

The problems with the *pro tanto* method are numerous and were thoroughly explored by the Ninth Circuit below. It allows the plaintiff to select which of several wrongdoers should bear the major burden of payment for a violation. This may be particularly inequitable in cases where the nonsettling parties are minor or peripheral participants in the wrongdoing and the settling defendants are the central actors.

As the Ninth Circuit found, under the *pro tanto* method,

> Plaintiffs may be tempted to engage in collusion with certain defendants. By accepting a low partial settlement, plaintiffs would be able to fund further litigation with no diminution of the total amount eventually received. Similarly, plaintiffs could effect low settlements with defendants who had limited resources, and thereby *force* wealthier defendants to pay more than if all parties proceeded to trial.

884 F.2d at 1230, Pet. App. at 17a-18a (footnote omitted).

Petitioners respond that there was no proof of collusion in this case, and that a low settlement with a culpable defendant will not harm the nonsettling defendants any

more than if the settling defendants went to trial and had no resources to pay a larger portion of the judgment. Every case is different, however, and the Ninth Circuit was concerned with the potential of the *pro tanto* method to provide an incentive for collusion and inequity.

Furthermore, an inequity can easily result under the *pro tanto* method where, as here, the inside participants in the alleged fraud settle for half their insurance coverage and leave the peripheral or secondary defendants, the auditor or the investment bankers, to bear the remaining exposure without recourse or contribution from the settling defendants.

Or a settlement could be *too favorable* with the settling defendant, and the nonsettling defendant could end up owing nothing, despite demonstrable culpability. This also could ultimately lessen the deterrent impact of the securities laws.[13]

Unlike the "proportional credit" method, where the risk of an inadequate settlement falls squarely on the parties who determine the terms of the settlement, the *pro tanto* approach places this risk on the nonsettling defendants—the parties whose statutory rights are being extinguished, but who have no power to control the terms of the settlement. Indeed, the rule invites abuse by plaintiffs, because a plaintiff's bargaining position is much enhanced by his ability to choose which defendant to hold responsible for most of his claim.[14]

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[13] *See Dobson v. Camden*, 705 F.2d 759, 766 (5th Cir. 1983), *rev'd on other grounds*, 725 F.2d 1003 (5th Cir. 1984) (*en banc*) (application of the *pro tanto* rule would contravene the deterrence goals of Section 1983 of the civil rights laws); Adamski, *Contribution and Settlement in Multi-party Actions Under Rule 10b-5*, 66 Iowa L. Rev. 533, 564 (1981) (hereinafter, "Adamski").

[14] "In a multi-party case the threat of an unshared judgment against the last remaining defendant—diminished only by meager settlements with his eager fellows—permits a plaintiff to create acute financial

The utilization of a "good faith" hearing does little or nothing to alleviate the drawbacks of the *pro tanto* method. First, pre-trial "good faith" hearings may waste judicial resources. If all of the parties ultimately settle, they would be bound by their settlement payments, and the adequacy of the payments made by each defendant would not be an issue. *First Fed. Sav. & Loan Ass'n of Pittsburgh v. Oppenheim, Appel, Dixon & Co.*, 631 F. Supp. 1029, 1037 (S.D.N.Y. 1986). Second, a subjective standard like "good faith" is difficult to define, creates uncertainty, and is almost immune from appellate review. Third, as the Ninth Circuit concluded, a properly conducted good faith hearing would require a precise determination of the parties' relative culpabilities. 884 F.2d at 1230, Pet. App. at 18a. The problems with conducting this procedure are apparent:

> [I]t would be unfair to expect that a decision like [determining the percentage of fault] could be made in anything resembling a summary procedure. Since the subtle determination of relative fault has such dramatic consequences, a fact finder would want to hear witnesses, judge demeanor and credibility, *etc.* No mechanism suggests itself except the equivalent of a full blown trial on the merits. Indeed, no one has suggested that the determination of the settling defendant's percentage share could be determined elsewhere but at the trial itself.

DeWolf, *Several Liability and the Effect of Settlement on Claim Reduction: Further Thoughts*, 23 Gonz. L. Rev. 37, 62 (1987).[15]

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pressures bordering on extortion." *River Garden Farms, Inc. v. Superior Court*, 26 Cal. App. 3d 986, 994, 26 Cal. Rptr. 458, 503 (1972); *accord* Stanford Note, *supra* note 12, at 490.

[15] Petitioners derive considerable comfort from the "good faith" hearing conducted by the trial court in this case. Pet. at 10. This hearing was conducted in accordance with the California state court practice established by *Tech-Bilt, Inc. v. Woodward-Clyde & Assoc.*, 38 Cal.3d

Under the "proportional credit" approach adopted by the Ninth Circuit in this case, the possibility of collusion between plaintiff and the settling defendant is almost nonexistent, and the nonsettling defendants' interests are completely protected. It is unlikely the plaintiff will settle for an intentionally low amount with one wrongdoer, knowing that any judgment against the remaining defendants will be reduced by the settling defendants' proportionate share of *total* damages. Thus, under the Ninth Circuit's approach, there is no need for the court to decide whether the settlement was made in good faith, only whether it is fair and reasonable to the absent class members.

The Ninth Circuit's approach is reflected in the most recent Uniform Act—the Uniform Comparative Fault Act (1977), 12 U.L.A. 39 (Supp. 1990) (the "1977 Uniform Act"). The NCCUSL concluded that neither the 1939 Uniform Act nor the 1955 Uniform Act was appropriate in a comparative fault system that based ultimate responsibility on the proportional fault of the parties involved. *Id.* at 40 (prefatory comment); *accord Dobson v. Camden*, 705 F.2d at 769.

The 1977 Uniform Act was therefore offered as a replacement whenever comparative fault principles have been adopted, such as in the federal securities laws. 1977 Uniform Act, 12 U.L.A. at 40 (Supp. 1990) (prefatory note); *see Smith v. Mulvaney*, 827 F.2d at 561. This approach

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488, 499 (1985). A California court is required to examine a number of factors, including the settling defendant's insurance coverage, to determine if the settlement is in "good faith." But, the court is *not* required to determine the settling defendant's relative culpability. All that is required is that the settlement be in the "reasonable range of the settling tortfeasor's proportional share of comparative liability for the plaintiff's injuries." *Id.* In the present case, the trial court was able to approve the settlement as being in "good faith," despite the fact that there was *no* evidence before it as to the relative culpability of the parties.

has been advocated by scholars, and has an extensive following in legislation and judicial decisions.[16]

The only benefit that petitioners can ascribe to the *pro tanto* rule is that it encourages *partial* settlements. Pet. at 13. Whether partial settlements are a worthwhile goal is debatable. The judicial system is still burdened with a case whenever a settlement is not complete. Judicial economy is greater when a plaintiff disposes of an entire case by negotiating collectively with all the defendants. Therefore, a policy that promotes *global* settlements fulfills a materially more important judicial goal. Fleming, *supra* note 16, at 1495; Stanford Note, *supra* note 12, at 489. In a case such as the instant one, for example, there is little benefit to be achieved from a settlement with the Kaypro Defendants since their conduct must still be litigated as the foundation for the liability of the other defendants.

The *pro tanto* rule, in fact, *discourages* global settlements. Because the plaintiff can continue to seek complete recovery after a partial settlement, the plaintiff is encouraged to negotiate piecemeal settlements to build a war chest to fund the prosecution of claims against defendants who may have little reason to be in the case except for the depth of their pockets. 884 F.2d at 1230, Pet. App. at 18a.

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[16] *E.g.*, N.Y. Gen. Oblig. Law § 15-108 (McKinney 1989); *United States v. Reliable Transfer Co.*, 421 U.S. 397 (1975) (maritime action); *Leger v. Drilling Well Control, Inc.*, 592 F.2d 1246, 1250 (5th Cir. 1979) (same); *Donovan v. Robbins*, 752 F.2d 1170, 1180-82 (7th Cir. 1985) (ERISA action); *Dobson v. Camden*, 705 F.2d at 763-71 (civil rights action); *Gomes v. Brodhurst*, 394 F.2d 465 (3d Cir. 1967) (negligence action); *In re Sunrise Securities Litigation*, 698 F. Supp. 1256, 1257-61 (E.D. Pa. 1988) (securities action); Fleming, *Report to the Joint Committee of the California Legislature on Tort Liability on the Problems Associated with American Motors Association v. Superior Court*, 30 Hastings L.J. 1464, 1494-1498 (1979) (hereinafter, "Fleming"); Adamski, *supra* note 13, at 551-54.

Under the Ninth Circuit's decision, although plaintiffs remain free to pursue a piecemeal settlement strategy, they are motivated to negotiate global settlements to minimize the risk of a mistaken assessment of the relative culpability of a settling defendant. Moreover, the plaintiffs are forced to focus their evaluation of a case on the real culpability of a defendant, rather than on a defendant's financial resources.[17]

The Ninth Circuit's decision encourages settlement in several other ways. It permits trial courts to satisfy the rights of nonsettling defendants to contribution prior to trial, thus cutting off claims against settling defendants. The express reason for granting this authority is to facilitate equitable partial settlements. 884 F.2d at 1229, Pet. App. at 16a. The rule also encourages total settlements after the execution of partial settlements. A nonsettling defendant can no longer escape financial responsibility based on its relative culpability merely because a settling defendant has paid more than its share. *See id.* at 1231, Pet. App. at 19a; *accord Dobson v. Camden*, 705 F.2d at 769.

Petitioners contend that the Ninth Circuit's rule discourages plaintiffs from reaching partial settlements by making the settlement too "dangerous" for them. Pet. at

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[17] This point is illustrated by petitioners' enthusiastic endorsement of the hypothetical under which they would recover $15.75 million of a $25 million judgment from defendants who are responsible for only 10% of the damages. Pet. at 9. The plaintiffs in such a situation are, of course, quite comfortable with their $25 million recovery. The settling defendants and their insurer are also pleased because they have paid only $9.75 million on a $25 million exposure and have saved over half of the $20 million insurance policy. The unfortunate parties in this scenario are the nonsettling defendants, who have to pay a $15.75 million judgment for which their proportionate share of the liability is only $2.5 million with no hope of recovering the difference from the settling defendants or their insurance carrier because the plaintiffs have successfully bargained with other parties to discharge those rights.

22. But, a settlement under the Ninth Circuit's rule is no more "dangerous" than any other settlement. Any diminution in the total recovery by a plaintiff is entirely the consequence of the plaintiff's decision to settle. Implicit in a plaintiff's decision to settle is the risk that more could be obtained through trial. Of course, the settling plaintiff is also eliminating the possibility of an adverse verdict. The risk that a plaintiff takes of misassessing these factors is present in *every* decision to settle.

The ultimate refutation of petitioners' unrelenting attack on the Ninth Circuit's decision is that the settlement they negotiated with the settling defendants contains a similar principle. The underlying Stipulation of Settlement provides that in the event of a successful appeal of the District Court's approval of the settlement by the nonsettling defendants, the settlement "shall convert to a reduction in judgment settlement" whereby any judgment against the nonsettling defendants "would be reduced by the amount of the Settlement . . . or by the amount of the Settling Defendants' share of the damages, *whichever is greater*." Pet. App. at 55a-56a (emphasis added). Thus, petitioners' agreement with the settling defendants expressly contemplates the possibility of the same outcome reached by the Ninth Circuit because, if the settlement were to be successfully attacked by the nonsettling defendants, the petitioners agreed that the settling defendants would nonetheless be released and the nonsettling defendants would not pay more than their proportionate share of the damages. This agreement is nothing more than a contractually negotiated version of the Ninth Circuit's proportional credit rule. In fact, as noted earlier, petitioners' Stipulation of Settlement contemplates a worse outcome for petitioners because the nonsettling defendants would receive a credit of the *greater* of the actual settlement *or* the settling defendants' share of liability.

In this context, petitioners' claim that "if the Ninth Circuit's rule had been known from the outset, plaintiffs

would not have settled with Kaypro and its eight officers and directors" seems disingenuous. Pet. at 22. As the Ninth Circuit recognized, "[a]n overwhelming majority of class action suits settle before trial." 884 F.2d at 1225, Pet. App. at 6a. For the past fifty-five years, securities actions have been settled by one of two methods. The first is with a contractually negotiated judgment protection clause such as that used by the petitioners and the settling defendants here.[18] The second method is by global settlement. Petitioners' attempt to portray the Ninth Circuit's decision as a radical departure from the *status quo* is not accurate, because the decision merely adopts a commonly used and effective settlement technique.

III

PETITIONERS DID NOT PROPERLY RAISE OR PRESERVE THE SECOND QUESTION PRESENTED

The second question presented by the petition is whether an implied right to contribution exists under Section 10(b) of the 1934 Act or under Section 12(2) of the 1933 Act. Petitioners assert that several federal courts of appeals have reached conclusions inconsistent with the Ninth Circuit's view that a right to contribution can be implied under these provisions of the federal securities laws. Petitioners, however, did not properly raise or preserve this question below.

Petitioners acknowledged to the Ninth Circuit that "[t]he issue of whether an implied right [of contribution] exists was not presented to or decided by the [district] court below." Appellees' Opposition Brief at 24 n.15. Petitioners, in fact, conceded before the Ninth Circuit that "an implied

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[18] For reported cases where a judgment reduction provision was a term of the settlement, *see In re Flight Transportation Corp. Securities Litigation*, 794 F.2d 318, 319 (8th Cir. 1986), *cert. denied*, 481 U.S. 1013 (1987); *Rose v. Associated Anesthesiologists*, 501 F.2d 806, 807 and n.2 (D.C. Cir. 1974) (medical malpractice case).

right to contribution [under the federal securities laws] is generally recognized," and petitioners "assume the existence of implied rights of contribution under these statutes . . . ." *Id.*

The first time petitioners asked any court to resolve the issue they now present to this Court was in their Petition for Rehearing in which they stated that "*if* the court rehears the case *en banc*, it can also determine whether there is an implied right to contribution under Section 10(b) . . . ." Petition for Rehearing with Suggestion for Rehearing *en banc*, p. 14 (emphasis added).

Raising an issue for the first time in a petition for rehearing is untimely. *Hoover v. Ronwin*, 467 U.S. 1268 (1984). Thus, the second question presented by the petition is simply unsuited for review by the Court. *Browning-Ferris Industries of Vermont, Inc. v. Kelco Disposal, Inc.*, ___ U.S. ___, 109 S. Ct. 2909, 2921 n.23 (1989); *Bankers Life & Casualty Co. v. Crenshaw*, 486 U.S. 71, 78 n.2 (1988); *Dothard v. Rawlinson*, 433 U.S. 321, 323 n.1 (1977).

Nor was this issue passed upon by the Ninth Circuit in this case. The court noted in passing that a right to contribution has been implied under Section 10(b) of the 1934 Act, without purporting to decide the issue itself. 884 F.2d at 1226, Pet. App. at 9a.[19] The court did not mention Section 12(2) of the 1933 Act at all.

Even if these issues had been timely raised below, there is no significant circuit conflict here. Every federal court of appeals that has considered the issue has concluded that there are implied contribution rights under Section 10(b)

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[19] The Ninth Circuit had concluded in another case that an implied right of contribution exists under Section 10(b) of the 1934 Act. *Smith v. Mulvaney*, 827 F.2d at 560. The question whether an implied right of contribution exists under Section 12(2) of the 1933 Act has not yet been decided by the Ninth Circuit.

of the 1934 Act.[20] Petitioners' citation of district court opinions on this issue does not change this fact.[21] The one circuit court that has declined to imply a contribution right under Section 12(2) of the 1934 Act does not present a serious conflict with the Ninth Circuit in this case where the Ninth Circuit simply did not address the issue in any context.

CONCLUSION

The principal issue presented for consideration by this Court in the petition for a writ of certiorari is not the subject of a conflict among the circuits and is still a developing issue in the district courts. The Ninth Circuit's

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[20] The Second, Fifth, Seventh and Ninth Circuits have implied a right of contribution under Section 10(b). *Sirota v. Solitron Devices, Inc.*, 673 F.2d 566, 578 (2d Cir.), *cert. denied*, 459 U.S. 838 (1982); *Globus, Inc. v. Law Research Service, Inc.*, 318 F. Supp. 955, 957-58 (S.D.N.Y. 1970), *result and reasoning aff'd without opinion*, 442 F.2d 1346 (2d Cir.), *cert. denied*, 404 U.S. 375 (1971); *Huddleston v. Herman & MacLean*, 640 F.2d 534, 556-59 (5th Cir. 1981), *aff'd in part, rev'd in part on other grounds*, 459 U.S. 375 (1983); *Heizer v. Ross*. 601 F.2d 330, 334 (7th Cir. 1979); *Smith v. Mulvaney*, 827 F.2d at 560.

[21] Pet. at 26 n.17. Petitioners also wrongly suggest that *Heizer Corp. v. Ross*, which implied contribution rights under Section 10(b), is no longer the law of the Seventh Circuit. *Id.* at 26. In *King v. Gibbs*, 876 F.2d 1275 (7th Cir. 1989), the Seventh Circuit considered whether it could imply *indemnification* rights under Section 10(b). In deciding this question, the court declined to follow the analytical approach it took in *Heizer* on the question whether to imply contribution rights under the same statute, because *Heizer* was decided before *Texas Industries, Inc. v. Radcliff Materials, Inc.*, 451 U.S. 630 (1981) and *Northwest Airlines, Inc. v. Transport Workers Union*, 451 U.S. 77 (1981). The Seventh Circuit, however, did *not* overrule *Heizer*. *Robin v. Doctors Officenters Corp.*, 730 F. Supp. 122, 124 (N.D. Ill. 1989). Moreover, other courts have implied contribution rights under Section 10(b) using the type of analysis called for by *Texas Industries* and *Northwest Airlines*, including at least one district court in the Seventh Circuit. *Eastern Holdings, Inc. v. The Illinois Co. Investments, Inc.*, 1989 U.S. Dist. LEXIS 8515 (N.D. Ill. 1989).

analysis and resolution of that issue was sound and should not be disturbed or even accepted for consideration at this time. The other question presented by the petition was, by petitioners' own admission, not timely raised or properly preserved below. Nor does it present a material conflict among the circuits. For these reasons, the petition should be denied.

Respectfully submitted,

*THEODORE B. OLSON
TERENCE P. ROSS
GIBSON, DUNN & CRUTCHER
1050 Connecticut Avenue, N.W.
Washington, DC 20036-5303
(202) 955-8500

**Counsel of Record*

Of Counsel:

LEONARD P. NOVELLO
General Counsel
JOHN A. SHUTKIN
Associate General Counsel
KPMG PEAT MARWICK
767 Fifth Avenue
New York, NY 10153

J. ANTHONY SINCLITICO, III
MARK J. MCKEON
GIBSON, DUNN & CRUTCHER
750 "B" Street, Suite 3300
San Diego, CA 92101-4605

Attorneys for Respondent KPMG Peat Marwick

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